Wyoming Lender Alert

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Making a Difference for Small Business in Wyoming

Checking Credit Reports & Scores

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Written by Edward A. Zurndorfer

Credit Reports and scores are growing in importance as more businesses use them for a variety of reasons. For example, during 2005, State Farm Insurance Company became the latest property casualty insurance company that uses a "credit scoring" model to determine premium rates for new automobile policyholders.

Businesses are also using credit checks to harness the "predictive power" of the data behind an individual's credit score. For example, cell phone companies have found that credit scores can be useful as predictors of which cell phone account holders are most likely to fall behind on their cell phone monthly payments.

What is a credit score and how is it computed? An individual's credit score is essentially a snapshot of the individual's credit worthiness at a particular time. Fair Isaac Corporation (located in California) created the most widely used credit score known as the FICO score. The FICO score ranges from a low of 300 (worst possible credit history) to a high of 850 (perfect credit history).

The Fair Isaac Corporation uses 22 types of data collected from the three major credit bureaus (Equifax, Experian and TransUnion) to calculate the credit score. The score is a composite from individual ratings in the following five categories.

1. Bill payment history (35 percent). Paying credit card bills and loans on time will result in higher FICO scores, missing payments or submitting the "minimum" each month will lower scores.

2. "Credit utilization" ratio (30 percent). Credit utilization refers to the credit balance to the credit limit ratio on credit card accounts (or the percentage of available credit being used on each card). Another term for the credit utilization level is "amounts owed." Maxing out credit cards will result in lowering one's FICO score; simply using 50 percent or more of credit limits can also cause problems. It is better if an individual has smaller balances (lower percentages) on several cards rather than piling up huge balances on one card.

3. Length of credit history (15 percent). It is a good idea to build up a lengthy credit use ("pay on time") credit history.

4. New accounts (10 percent). Consistently applying for new lines of credit raises "red flags" because it makes the consumer look riskier. It is therefore a good idea to avoid the home equity "lines of credit" or store retailer cards.

5. Types of credit (10 percent). Consumers get credit for owning a variety of loans, including auto loans or mortgages compared to owning only credit cards.

Note that an individual's income is not a factor in determining his or her FICO score. An individual may have a high income, but that does not mean that he or she pays credit card bills on time.

To see what effect on interest rates a lower or higher FICO score has, consider the following example (from Inform Research Services, Inc.) of a $350,000 mortgage and varying interest rates.

Note the varying interest rates and resulting monthly payment (principal and interest) amounts depend on the FICO score range.

Mortgage rates on a $350,000 mortgage

FICO SCORE	Annual Percentage Rate*	Monthly Payment	Total Interest
720-850	6..24%	$2,153	$424,984
700-719	6.37%	$2,181	$435,252
675-699	6.90%	$2,306	$480,005
620-674	8.05%	$2,2581	$579,115
560-619	8.53%	$2,699	$621,601
500-559	9.29%	$2889	$690,134

*Rates as of Nov. 11 Data: Informs Research, Inc. www.myfico.com

What should individuals do to check their credit scores? Here are some suggestions. (Note that in the case of a married couple, each spouse should check both his and her credit reports and credit scores.)

Check credit reports from the three major credit reporting agencies. As the FICO score is based on information in credit reports, it is important for individuals to check their reports to make sure they are complete. Credit reports can sometimes contain errors. The Fair and Accurate Transaction Act of 2003 entitles every individual to a free credit report from each of their major credit reporting agencies once a year. Reports can be ordered online at www.annualcreditreport.com.

Obtain FICO credit scores. To do this, one should go to www.myfico.com. A score from one of the major credit reporting agencies will cost $14.95; scores from all three reporting agencies will cost $44.85. It is advisable to purchase FICO scores from all three credit bureaus because large lenders either average the three credit scores or take the middle score.

Important Reasons To Love Wyoming Small Business

The Heart of the State's Economy

Small businesses are the heart of Wyoming's economy and the Office of Advocacy of the U.S. Small Business Administration. We are sending this with the reasons to love them.

10. Small businesses make up 96.6 percent of all Wyoming employers.

9. Small businesses create more than 50 percent of the American nonfarm private gross domestic product (GDP).

8. Small patenting firms produce 13 to 14 times more patents per employee than large patenting firms.

7. The 56,740 small businesses in Wyoming are located in every community and neighborhood.

6. Small businesses employ 69.3 percent of Wyoming's non-farm private sector workers.

5. Home-based businesses account for 53 percent of all small businesses.

4. Small businesses are 97 percent of America's exporters and produce 26 percent of all export value.

3. Wyoming saw an estimated 2,519 new small firms with employees start-up in the last year measured.

2. There are approximately 2,500 minority-owned businesses and 12,946 women-owned businesses in Wyoming, and almost all of them are small businesses.

1. The latest figures show that small business creates 65 percent or more of America's net new jobs.

The Office of Advocacy, the "small business watchdog" of the government, examines the role and status of small business in the economy and independently represents the views of small business to federal agencies, Congress, and the President. It is the source for small business statistics presented in user-friendly formats and it funds research into small business issues.

Top Ten Reasons for Repair, Denial of the SBA Guarantee

Reprinted Courtesy of
NAGGL January "InFocus" Issue
Written by of Lucy Gardner Davis

The SBA guarantee purchase has changed dramatically over the last three years. As lenders increasingly centralized their functions, the SBA followed suit and created the National Guarantee Purchase Center (NGPC) located in Herndon, Virginia. The NGPC has a very helpful website that assists lenders in navigating their way through the guarantee purchase process. See: http://www.sba.gov/banking.ngpc/

If the SBA finds a material deficiency during the review of a guarantee purchase request, they will either negotiate a repair of the guarantee or completely deny liability under the guarantee. This article outlines some of the most common reasons for a repair or denial of liability under the guarantee.

1. **Loan has matured and 120 days have passed since maturity.** This may arise when a lender has an older loan that has gone into default and the liquidation is taking a long time. If warranted, the SBA may grant a reinstatement if the guarantee and extension of the maturity as an exception to policy that must be approved by the SBA Headquarters. (Please note: Proposed SBA regulation 13 CFR § 120.524 would increase this time limitation to 180 days.)

2. **Failure to properly secure and perfect a lien on collateral.** For example, the loan is secured only by real estate and the lien is not valid due to failure of the lender to properly perfect the lien.

3. **Failure to properly document a Borrower's injection on a start-up business that went into liquidation within 18 months of final disbursement.** If the required injection is asset based, the lender should provide a list of the assets along with an appraisal. If the injection is monetary, the lender should provide cancelled checks and the borrower's bank statement dated *prior* to the loan closing date.

4. **Failure to show use of proceeds in accordance with the Loan Authorization.** The SBA Settlement Sheet Form 1050 requires that lenders use joint payee checks to ensure that proceeds are used according to the Authorization. If the lender does not use joint payee checks, they should use invoices marked 'paid', supported by copies of cleared checks or bank statements showing that the checks cleared. Procedural Notice 5000-562 also requires a detailed list of all personal property with a value of over $5,000 purchased with loan proceeds.

5. **Failure to close or service the loan in a prudent manner causing a loss to the agency.** One example of imprudent servicing would be the failure to obtain a legally enforceable note because the wrong party signed.

"It is important to provide a complete package in accordance with the SBA checklist and to work closely with the SBA loan officer…"

6. **Failure to liquidate the collateral in a prudent manner.** When the loan goes into default, the lender should perform a site visit in accordance with SOP 50-51. If a lender does not act quickly to liquidate the collateral, it is possible that the borrower can abscond with the collateral, or that the collateral's value will be decreased due to neglect.

7. **Failure to obtain life insur-ance per the Authorization requirements and the death of a principal causes the failure of the business.** In this case, the SBA will likely repair in the amount of the life insurance policy as required in the Authorization.

8. **Early default with failure to provide evidence of verification of tax returns through IRS Form 4506.** Since October 1994, the SBA has required the verification of all tax returns through use of IRS Form 4506. If the business fails within eighteen months of the loan closing, and the lender cannot provide the IRS Form 4506 showing verification of the tax returns, it will be incumbent on the lender to provide information that shows that the business failure was due to factors that could not have been identified through the verification process.

9. **For PLP Lenders, the loan was ineligible for an SBA guarantee.** If a loan was made to an entity that is not eligible for SBA financing under 13 CFR § 120.110 (such as, a non-profit organization or a religious-affiliated organization), the SBA cannot honor its guarantee. Additionally, the SBA will consider a denial of liability under its guarantee if a franchise agreement is not on the franchise registry and is considered ineligible 13 CFR § 121.103(i).

10. **For PLP Lenders, the guarantee of a twenty percent or more owner**

of the company was not obtained. Under 13 CFR 120..110(3), the SBA has a six-month look-back rule in determining ownership of a company. It is important to determine all of the owners within that six-month window in order to obtain the guarantee of any individual who has a 20% or greater interest.

The items on this list are not exhaustive. Most of the time, if a lender can mitigate the loss to the Agency, the repair will be minimal. It is important to provide a complete package in accordance with the SBA checklist (see www.nagle.org/resources) and to work closely with the SBA loan officer reviewing your guarantee purchase package.

Mapping Your Path with a Business Plan

You wouldn't start out on a cross-country trek without a map, so why would you want to try to start a business without a business plan?

A business plan precisely defines your business, identifies your goals, and serves as your firm's resume. It helps you allocate resources properly, handle unforeseen complications, and make good business decisions. Because it provides specific and organized information about your company and how you will repay borrowed money, a good business plan is a crucial part of any loan application. Additionally, it informs sales personnel, suppliers, and others about your operations and goals.

The importance of a comprehensive, thoughtful business plan cannot be overemphasized. One of the greatest benefits is that putting a plan together forces you to sit down and map out exactly how you expect to make your business idea successful. Much hinges on it: outside funding, credit from suppliers, management of your operation and finances, promotion and marketing of your business, and achievement of your goals and objectives.

Despite the critical importance of a business plan, many entrepreneurs drag their feet when it comes to preparing a written document. They argue that their marketplace changes too fast for a business plan to be useful or that they just don't have enough time. However, just as a builder will not begin construction without a blueprint, eager business owners should not rush into new ventures without a business plan.

There are four core questions to answer before you begin writing your business plan.

1) What service or product does your business provide and what needs does it fill?

2) Who are the potential customers for your product or service and why will they purchase it from you?

3) How will you reach your potential customers?

4) Where will you get the financial resources to start your business?

Although there is no single formula for developing a business plan, some elements are common to all business plans. Your plan should start with a cover sheet, a statement of your business purpose and a table of contents. Then start with a section about your business idea: describe your business, tell how you plan to market it, review your competition, describe the operating procedures you plan to adhere to, discuss your plans for employees, and how you plan to hire and train them, and describe your approach to insuring the business.

Next, you will want to provide detailed financial data, including any loan applications you will file, a list of the equipment and supplies you will need and how much they will cost, a balance sheet showing your assets and liabilities, an analysis of what it will take for you to break even, and a projection of your business' income, including anticipated profits and losses.

Your financial data should also be organized in a three-year summary, with detailed projections of cash flow, costs and income, organized month-by-month for the first year and quarter-by-quarter for the second and third years. Be sure to include a discussion of the assumptions on which your projections are based.

You should also have an executive summary in which you summarize the plan, and be prepared to attach supporting documents and financial projections. The supporting documents should include resumes and tax returns of the principal owners for the previous three years, a copy of a franchise agreement if your business is a franchise, copies of proposed leases or purchase agreements for business space, copies of licenses and other legal documents, and copies of letters of intent from suppliers and known customers.

You can find a detailed guide to producing a solid business plan on the SBA website at www.sba.gov/wy/indes.html and select SBA/SCORE Resource Guide

Did you know?

In a recent study titled "Survival and Longevity in the Business Employment Dynamics Database", by Amy E. Knaup, Monthly Labor Review, Volume 128, Number 5 (May 2005), it was found that two-thirds of new employer establishments survive at least two years, and 44 percent survive at least four years.

Upcoming Events

March 1– Women's Roundtables Casper/Dubois

March 2 – Women's Roundtable Jackson

March 9 – Women's Roundtables Laramie and Worland

March 16 – Women's Roundtable Powell

March 21 – Women's Roundtable Cody

March 22– Native American Business Expo

March 25 – Johnson County Business Expo